CONSULTATION ON THE REVISION OF THE EU EMISSION TRADING SYSTEM (ETS) DIRECTIVE

1. Free allocation and addressing the risk of carbon leakage

1.1 The European Council called for a periodic revision of benchmarks in line with technological progress. How could this be best achieved in your view and, in particular, which data could be used to this end? How frequently should benchmarks be updated, keeping in mind administrative feasibility?

The ETS is the cornerstone of EU climate policy and the Netherlands is of the opinion that it is of utmost importance to strengthen it. This does not only involve tightening the cap so that a significant price signal towards sustainable innovation is created, but it is important to look at the complete picture and also evaluate important aspects like free allocation and benchmarking.

The current product benchmarks are outdated, they are not representative for the period 2021-2030. Before the start of the next trading period the product benchmarks should be revised to reflect the current GHG-efficiency in the EU.

As a starting point one must determine the benchmark improvement during the current trading period as well as estimate the improvement in coming years. In order to achieve this, the roadmaps developed by the industry sectors themselves should be used to come to more realistic benchmarks.

The benchmarks can again be set for the entire trading period from 2021 onwards, but with an improvement factor. This factor should be based on the exogenous technological improvement seen for that particular production process. It is key that the benchmarks will not be updated too often. Not only for administrative reasons. Another important reason is that it would otherwise reduce the incentive for industry to take technical measures, because they would not get the (full) benefit for cleaner production.

The administrative burden could be lowered significantly by introducing more product-benchmarks. This would also result in more equal treatment between different installations in a sector.

1.2 The European Council has defined guiding principles for the development of post-2020 free allocation rules which provide inter alia that "both direct and indirect costs will be taken into account, in line with the EU state aid rules" and that "the most efficient installations in these sectors should not face undue carbon costs leading to carbon leakage" while "incentives for industry to innovate will be fully preserved and administrative complexity will not be increased" and while "ensuring affordable energy prices". Do you have views how these principles should be reflected in the future free allocation rules?

The principles can best be reflected in an adjusted free allocation system, as elaborated in our reaction to the previous written consultation. The industry sectors that face a real carbon leakage risk should be granted one hundred percent free allocation based on recent production and realistic benchmarks. The free allocation should take into account direct as well as indirect carbon costs. Direct and indirect emissions both have to be addressed in the carbon leakage context since the costs of both types of emissions have the same economic effects. A solid and predictable alternative for the diverse, unstable and incomplete system of compensation on MS level currently in place could be: an EU-wide scheme for allocation related to indirect emissions with boundaries set in the ETS-directive.

To ensure that the administrative complexity will not increase, but decrease, further use of product benchmarks is needed. Moreover, one could think of a system that periodically, for instance every three years, makes adjustments for the adjusted production levels of a company.

With such a system in place, we see no justification for the application of any additional correction factor to calculate the free allocation for installations. The application of a correction factor under these circumstances would be contrary to the objective of the development of a robust carbon leakage scheme, in which the most vulnerable sectors are adequately protected against carbon leakage.

The current complexity of the system and the thick rule book for allocation result mainly from rules to account for any changes between the historical base period and now. This in itself provides a good argument for a method of allocation based on actual production. This would also help to solve the problem that, as we have seen, the current rules encourage strategic behavior around the thresholds for cessation, to get more allowances than actually needed.

1.3 Should free allocation be given from 2021 to 2030 to compensate those carbon costs which sectors pass through to customers? How could free allocation be best determined in order to avoid windfall profits?

In principle, carbon costs that can be passed through to customers should not be compensated for.

It is quite possible there are sectors that can't fully pass through their costs without losing market share. This can be taken into account when changing the carbon leakage criteria. Windfall profits should be prevented along two lines:

1. Only industries that suffer from carbon leakage should be fully compensated for the direct and indirect costs. As stated in our reaction to the previous consultation, the carbon leakage criteria can be improved and the CO_2-price used for the calculations should be updated periodically. For instance a more realistic carbon price could be applied that could be partially based on the current carbon price and partially on an estimated future carbon price.

   We've also put forward the idea of having a tiered system for free allocation, which would mean that sectors that are not facing a risk of 100% carbon leakage, do not necessarily need to receive 100% free allocation. On the other hand this could further increase the complexity of the system, so care should be taken when designing this tiered sytem.

2. Allocation of allowances to prevent carbon leakage should be matched with real production volumes in order to prevent overcompensation as a result of decreasing production amounts. This way of allocating should also prevent new surpluses to appear.

1.4 Are there any complementary aspects you would like to add to the replies given to the previous written consultation in the light of the European Council conclusions?

The European Council conclusions decided on the introduction of a market stability reserve. An option under discussion is that the backloaded allowances and other spare allowances flow directly into the MSR. As part of these allowances were originally for allocation to industry, we think (part of the) allowances from the MSR can later flow into an allocation supply reserve. The allocation supply reserve could be introduced to guarantee that a system that best reflects the Council Conclusions on free allocation, functions under the ETS cap.

Additionally, it should be ensured that the Council Conclusions' referral to better reflect changing production levels in a reformed ETS is not misunderstood as some form of adapted closure and new entrance rules (as this would lead to even more administrative complexity) but as allocation based on recent production levels.

2. Innovation fund: NER 400

2.1 Do you see reasons to modify the existing modalities applied in the first two calls of the NER300? Are there any modalities governing the NER 300 programme which could be simplified in the design of the innovation fund? If you see the need for changes, please be specific what aspects you would like to see changed and why.

Since the NER is such a large fund, the managing of this fund should be fully transparent. We would also like to see more transparency in the assessment project proposals go through. The assessment of projects under the NER300 was a black box and seemed to lead to suprising outcomes. We think that this process should be guided by clear predefined criteria. In the present, NER projects are evaluated as being standard engineering projects, while we think that for innovation projects another approach is needed.

We would like the NER400 to be more flexible than the NER300. Because of the long periods before the commissioning of a project, it might be necessary to change some features of the project (for instance, using new techniques) in the process. It should be possible to incorporate revisions in projects, even after they have been awarded a subsidy from the NER.

In general, positive investment signals depend on a range of policies not just the EU ETS or NER300, and therefore a coherent and coordinated approach will be indispensable to tackle the question of how regulatory certainty can be improved.

One of the principle aims of the NER300 was to promote CCS. This did not succeed as was intended, because CCS-projects in the NER300 were obliged to conform to (too) strict criteria (only in certain installations, certain size). For achieving the long term objectives of EU climate policies, strong focus on CCS is still necessary. We think that a broader range of CCS-projects should also be eligible. For instance projects in which the CO_2 is captured and used in industry or mining, or projects that combine CCS with a biomass plant.

We think that the aim of the NER400 should be at innovative techniques, and not at the deployment of already used techniques, like regular deployment of renewable energy production units. It should also be possible to support innovative low carbon projects in industry.

2.2 Do you consider that for the extended scope of supporting low-carbon innovation in industrial sectors the modalities should be the same as for CCS and innovative renewable energy technologies or is certain tailoring needed, e.g. pre-defined amounts, specific selection criteria? If possible, please provide specific examples of tailored modalities.

The development of new technologies follows a pre-defined path (from development to deployment and commercialisation) where different types and levels of support are needed in the different stages. It is important to adequately define the appropriateness of each type of aid. Support is principally necessary at each stage in order to overcome the market barriers and failures specific to each stage. We see a particular lack of support for large scale pilots in industries and would wish to have the EU more active here.

We think that projects qualifying for the NER400 should be really break-through projects that Europe could play a leading role in; technologies that could bring great economic opportunities and make Europe the frontrunner in a specific field. CCS is a good example of this, but for this time is running out.

It would be good to let the NER400 connect to all the work that is done under the Horizon 2020 programme and we think that similar (improved) modalities should applied for the non-CCS projects as for CCS-projects under the NER400.

2.3 Are there any complementary aspects regarding innovation funding you would like to add to the replies given to the previous written consultation in the light of the European Council conclusions?

From our point of view, a bottleneck in the commissioning of CCS projects is the financial uncertainty in the unlikely case of leakage of CO_2 from a CCS site. For the amount of CO_2 leaked, CO_2-allowances should be handed over, but financing partners of CCS-projects are not able to insure this fact because of the uncertainty in the CO_2-price.

3. Modernisation fund

The European Council has concluded that 2% of the total EU ETS allowances in 2021 to 2030 should be dedicated to address the particularly high investment needs for Member States with GDP per capita below 60% of the EU average. The aim is to improve energy efficiency and to modernise the energy systems of the benefitting Member States. The fund should be managed by the beneficiary Member States, with the involvement of the European Investment Bank (EIB) in the selection of projects.

3.1 Implementation of the modernization fund requires a governance structure: What is the right balance between the responsibilities of eligible Member States, the EIB and other institutions to ensure an effective and transparent management?

The beneficiary Member States will manage the fund, as stated in the Council Conclusions. The Council Conclusions do not foresee any additional EIB funding. It is also the position of the Dutch Government that there is no need for additional funding coming from the EIB. The EIB should, however, be asked to do an extensive due diligence, as part of its involvement in the selection of projects. This due diligence should be as strict as a due diligence for a project with EIB funding. On the basis of the EIB due diligence, the European Commission would have a final say in whether the project is viable or not. This ensures that only high quality projects are selected, that no crowding out of market funding takes place and that funding contributes to the goal of improving energy efficiency and modernising energy systems in the beneficiary Member States.

3.2 Regarding the investments, what types of projects should be financed by the modernisation fund to ensure the attainment of its goals? Should certain types of projects be ineligible for support?

Projects should fit in the transition towards a sustainable economy and should avoid any carbon lock-in. We prefer investments in renewable energy projects that focus on a transition from coal to biomass. Nevertheless, the funds should not be used for exploitation of renewable energy (no subsidies for kWh production), but for key modernisations which make the old networks suitable for large amounts of renewable energy. Therefore it should be related to the goals as set by the infrastructure package. For a more sustainable use of energy it is also important to invest in heat networks.

3.3 Should there be concrete criteria [e.g. cost-per-unit performance, clean energy produced, energy saved, etc.] guiding the selection of projects?

All projects should meet some cost-effectiveness criteria, aimed towards the goal of a more sustainable economy. Thus projects that are capable of reducing CO_2 in a cheaper way and are also smart investments for the desired transition should be favored. On the other hand, we are aware cost-effectiveness criteria are hard to define for these kind of modernization projects.

No overstimulation should take place (no accumulation of subsidies).

3.4 How do you see the interaction of the modernisation fund with other sources of funding available for the same type of projects, in particular under the optional free allocation for modernisation of electricity generation (see section 4 below)? Would accumulation rules be appropriate?

Market parties are primarly responsible for investments in (the modernisations of) generation capacity. Interaction can happen. Setting accumulation rules is appropriate. Accumulation should not lead to any form of overstimulation. So for instance with RES subsidies, it should not be possible to apply for a national scheme and on top of that apply for this modernization fund.

Accumulation of funds from the modernisation fund combined with free allocation to promote investments in modernizing the energy sector is possible, but should not lead to overstimulation.

3.5 Do you have views how the assessment of the projects should be reflected in the forthcoming 2030 governance process (e.g. national climate programmes, and plans for renewable energy and energy efficiency)?

It is important that the supported projects are well in line with the different national transition processes towards a sustainable economy, therefore we support the idea to link it to the 2030 governance process.

3.6 Should the level of funding be contingent on concrete performance criteria?

The transition towards a more modern and sustainable economy is not an easy process. Therefore, funding should give a significant amount of financial security to the projects. Nevertheless, when it is very clear that projects are not performing as they are supposed to, it should be possible to take corresponding measures.

4. Free allocation to promote investments for modernising the energy sector

4.1 How can it be ensured that investments have an added value in terms of modernising the energy sector? Should there be common criteria for the selection of projects?

In principle the energy sector should not be subject to carbon leakage, therefore, the Netherlands believes that in the long run they should not receive free allocation anymore. Therefore the allowances that will be handed over in the next trading period, should aim at modernizing the energy sector to such an extent that future free allocation to the energy sector will no longer be necessary.

4.2 How do you see the interaction of the free allocation to energy sector with other sources of funding available for the same type of projects, e.g. EU co-financing that should be made available for the projects of common interest under the 2030 climate and energy framework? Would accumulation rules be appropriate?

The ETS should in principle not become a source of income to be spent on other purposes but instead the ETS market should drive the achievement of agreed emission reductions at the lowest cost.

That said, when interaction with other sources of funding is possible, setting accumulation rules is appropriate. No accumulation should take place when this could lead to overstimulation.

4.3 Do you have any views how the assessment of the projects should be reflected in the forthcoming 2030 governance process (e.g. as regards improving transparency)?

Stakeholders should be consulted early in a transparent fashion and projects should be peer-assessed by independent reviewers.

4.4 The maximum amount of allowances handed out for free under this option is limited. Do you think eligible Member States should use the allowances for a period of time specified in advance (e.g. per year), or freely distribute them over the 2021-2030 period? (Please explain your motivation.)

We prefer this option for a period of time specified in advance. This gives more certainty to market participants at when the allowances come to the market.

4.5 Should there be priorities guiding the Member States in the selection of areas to be supported?

- [x] **yes**
- [ ] no

If so, which of the following areas, if any, currently supported through investments for modernisation of electricity generation up to 2020 should be prioritised for support up to 2030 and why?

- ☐ Interconnectors
- ☐ Smart Grids
- ☐ Super-critical coal
- ☐ Gas
- ☐ Renewable energy
- ☐ Energy storage
- ☐ Energy efficiency
- ☐ Other (please elaborate)

Please explain in detail:

The funding should be awarded to the real bottlenecks that impede the modernizations that are necessary in the trajectory towards a sustainable economy. Furthermore member states should coordinate with neighboring countries in order to promote further establishment of the internal energy market of the EU.

4.6 How can improved transparency be ensured with regard to the selection and implementation of investments related to free allocation for modernisation of energy? In particular regarding the implementation of investments, should allowances be added to auctioning volumes after a certain time period has lapsed in case the investment is not carried out within the agreed timeframe?

The member states can report about the foreseen investements and investements already taken. If allowances haven't been spent, they should come to the market by way of auctioning.

5. SMEs / regulatory fees / other

5.1 Are there any EU ETS administrative requirements which you consider can be simplified? Do you see scope to reduce transaction costs, in particular for SMEs? If yes, please explain in detail.

Yes. The Dutch Emissions Authority is investigating the possibilities for simplifying the EU ETS. The aim is to identify measures that reduce administrative burden, without undermining the credibility of the system. Their interim report will be published end of April. They consider there are at least four chances of reducing the administrative burden of the EU ETS:

- Handle accuracy, risks and safety in a more proportional way
  Examples:
  - introduce for small companies default values for complex process emissions and allow calculation of emissions on gas/fuel account;
  - introduce risk-based approaches for the periodic review of permits and KYC-documents;
  - make the IT-security of the registry commensurate with the risks.

- Increase usability and service
  Examples:
  - make templates better understandable and more user friendly;
  - allow and enable an automated surrendering of allowances.

- Review some of the exceptions
  Examples:
  - reconsider the complex participation criteria;
  - try limiting the use of the fall back option for free allocation (the complicated heat benchmark) by introducing more product benchmarks;

- Reconsider the entry-criteria, with special concern for the burden for the 30% smallest emitters that cover only 0,70% of the total emissions
  Examples:
  - exclude installations which rarely use their capacity by basing the entry-criteria on emissions instead of capacity;
  - reconsider the wording of the opt out provision in order to make it easier in practice to exclude small emitters;
  - allow the opt out of small installations during a trading period.

5.2 Member States had the possibility to exclude small emitting installations from the EU ETS until 2020. Should this possibility be continued? If so, what should be the modalities for opt-out installations to contribute to emission reductions in a cost-effective and economically efficient manner? Should these be harmonised at EU level?

Yes, this possibility should be continued. The wording of the provision should be reconsidered in order to make it easier to opt out in practice. The experiences that Member States have on this in practice can be used.

5.3 How do you rate the importance of a high level of security and user-friendliness of the Union Registry? Do you think the costs for providing these services should be covered via Registry fees?

Security in the Union Registry is of vital importance. However, some of the security measures imposed after the 2011 fraud cases, seem disproportional. The balance between security and user-friendliness should and can be restored. Possible changes include improving the user interface, functionality for automating the surrendering of allowances, shortening the waiting period for accounts to be added to the trusted account list and introducing an compliance account without trading facilities (and thus with less IT-security). We could discuss using registry fees to speed up such developments in the Union Registry. However, this should then be part of a wider discussion about the development of the registry, the change management and the fee structure.

5.4 Do you consider discrepancies in Registry fees in different Member States justified? Should Registry fees be aligned at EU level?

The Registry fees should remain a matter of national policy. Determining their own registry fees allows Member States to establish the level of service they provide accordingly.

5.5 Under the current EU ETS Directive, at least 50% of the revenues generated from the auctioning of allowances should be used by Member States for climate-related purposes. For the calendar year 2013 Member States have reported to have used or to plan to use 87 % on average to support domestic investments in climate and energy. Do you consider the current provisions regarding the use of the revenues adequate for financing climate action? If not, please explain why?

Yes, although we emphasize that we have a clear separation between public income and public spending.

6. General evaluation

6.1 How well do the objectives of the EU ETS Directive correspond to the EU climate policy objectives? How well is the EU ETS Directive adapted to subsequent technological or scientific changes?

The main objective, the reduction in carbon dioxide emissions, corresponds well to the climate objectives. As the carbon price was much lower than expected, mainly on account of the economic crisis, stimulating the use of cleaner technology was less than envisioned. By strengthening of the EU ETS (higher reduction percentage, MSR and better carbon leakage protection) we think the ETS can also correspond much better with that objective. For us it's clear this should be done as regards to carbon leakage protection with an allocation system based on recent/actual production volumes and realistic benchmarks, with no need for additional correction factors.

Furthermore, it is important to make sure that ETS is well in tune with the other climate, energy and environmental policies.The MSR can help alleviate effects from other policies towards the ETS, but the ETS stays sensitive to technological and scientific changes. To better accommodate this, we think that the system should be updated more often.

6.2 What are the strengths and weaknesses of the EU ETS Directive? To what extent has the EU ETS Directive been successful in achieving its objectives to promote emission reductions in a cost-effective manner compared to alternatives, e.g. regulatory standards, taxation?

The main strength of the ETS is that it reduces carbon dioxide emissions in the whole of Europe in a cost effective way, without changing the level playing field inside Europe. The desired reductions are always met.

A weakness is that the EU ETS is still not a global instrument. This means that we still need to pay attention to the risk of carbon leakage.

Another weakness is that additional measures on energy saving don't bring the carbon dioxide emissions down during a set trading period.

Besides that, the role of ETS in supporting breakthrough technologies has been modest.

6.3 To what extent are the costs resulting from the implementation of the EU ETS Directive proportionate to the results/benefits that have been achieved, including secondary impacts on financing/support mechanisms for low carbon technologies, administrative cost, employment impacts etc.? If there are significant differences in costs (or benefits) between Member States, what is causing them?

In our opinion the costs are proportionate for the majority of installations. The costs aren't always proportionate for smaller installations. Although the EU ETS could be a very straight forward system, it has become quite complex. The administrative burden for participating companies (especially the smaller ones) compromises the cost-effectiveness of the EU ETS and undermines the support for the system. Simplification is required to make the EU ETS future-proof.

We don't have insight in the costs and benefits differences between Member States.

6.4 How well does the EU ETS Directive fit with other relevant EU legislation?

The EU ETS is well embedded as a cornerstone of EU climate policy. Nevertheless, interaction with other climate, energy and environmental legislations impacts the EU-ETS. This is not necessarily a problem, but there is a need to closely monitor the interactions, therefore this should be taken into account in the design process and tin the impact assessments of future related legislation. We think the MSR can (partially) improve the dealing with these interactions.

6.5 What is the EU value-added of the EU ETS Directive? To what extent could the changes brought by the EU ETS Directive have been achieved by national measures only?

The EU value-added of the directive is that it guarantees harmonization and a level playing field on European level. Before the EU ETS came into play, the Netherlands had it's own plans for developing an national emissions trading system. It's hard to tell if that or other measures would have achieved the same results.

6.6 Do you have any other comment on the revision of the EU ETS Directive that you would like to share?

The carbon price did not reach the levels that were anticipated. We hope that the revised EU ETS will entail a more stable and robust carbon price signal.

Unfortunately, the EU ETS is still not a global instrument. This means that we still need to pay attention to the risk of carbon leakage (including the risk that new investments are not undertaken; investment leakage) and take measures to tackle this risk. However there is a growing amount of international and regional ETS schemes, these developments need to be taken into consideration when developing carbon leakage criteria.

Under the Lisbon Treaty, regulatory comitology procedure with scrutiny is no longer possible. We believe that the new revised directive should address as detailed as possible all the elements that were mentioned in the October Council Conclusions (carbon leakage framework, allocation rules).